

Decatur County Hospital
A Component Unit of Decatur County, Kansas
Accountants' Report and Financial Statements
December 31, 2010 and 2009



Decatur County Hospital
A Component Unit of Decatur County, Kansas
December 31, 2010 and 2009

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Independent Accountants' Report on Financial Statements and Supplementary Information

Board of Trustees
Decatur County Hospital
Oberlin, Kansas

We have audited the accompanying balance sheets of Decatur County Hospital, a component unit of Decatur County, Kansas, as of December 31, 2010 and 2009, and the related statements of revenues, expenses and changes in net assets and cash flows for the years then ended. These financial statements are the responsibility of the Hospital's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the Kansas Municipal Audit Guide. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Decatur County Hospital as of December 31, 2010 and 2009, and the changes in its financial position and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

The Hospital has not presented management's discussion and analysis that the Governmental Accounting Standards Board has determined is necessary to supplement, although not required to be a part of, the basic financial statements.

Our audits were conducted for the purpose of forming an opinion on the Hospital's basic financial statements. The accompanying supplementary information as listed in the table of contents is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the basic financial statements taken as a whole.

BKD, LLP

April 12, 2011

Decatur County Hospital
A Component Unit of Decatur County, Kansas
Balance Sheets
December 31, 2010 and 2009

Assets

	2010	2009
Current Assets		
Cash and cash equivalents	\$ 723,391	\$ 610,031
Short-term certificates of deposit	509,948	509,948
Patient accounts receivable, net of allowance; 2010 - \$402,000, 2009 - \$372,000	1,268,570	835,233
Current maturities of notes receivable	15,654	19,670
Other receivables	9,941	59,992
Estimated amounts due from third-party payers	-	480,000
Supplies	104,962	89,511
Prepaid expenses and other	47,974	30,578
	<hr/>	<hr/>
Total current assets	2,680,440	2,634,963
	<hr/>	<hr/>
Noncurrent Cash		
Held by trustee for debt service	48,786	48,786
	<hr/>	<hr/>
Investments and Long-term Deposit		
Interest in assets of Decatur Health Care Foundation, Inc.	2,041,762	1,881,348
Option deposit	250,000	250,000
	<hr/>	<hr/>
	2,291,762	2,131,348
	<hr/>	<hr/>
Capital Assets, Net	1,712,995	1,705,794
	<hr/>	<hr/>
Other Assets		
Notes receivable	-	16,092
Deferred financing costs	6,750	7,125
	<hr/>	<hr/>
	6,750	23,217
	<hr/>	<hr/>
Total assets	\$ 6,740,733	\$ 6,544,108
	<hr/>	<hr/>

Liabilities and Net Assets

	2010	2009
Current Liabilities		
Note payable to bank	\$ -	\$ 150,000
Current maturities of long-term debt	54,461	53,044
Accounts payable	155,695	228,585
Accrued expenses	488,404	438,851
Estimated amounts due to third-party payers	278,834	-
	<hr/>	<hr/>
Total current liabilities	977,394	870,480
Long-term Debt	<hr/>	<hr/>
	626,506	680,967
Total liabilities	<hr/>	<hr/>
	1,603,900	1,551,447
Net Assets		
Invested in capital assets, net of related debt	1,032,028	971,783
Restricted - expendable for debt service	48,786	48,786
Unrestricted	4,056,019	3,972,092
	<hr/>	<hr/>
Total net assets	5,136,833	4,992,661
Total liabilities and net assets	<hr/> <hr/>	<hr/> <hr/>
	\$ 6,740,733	\$ 6,544,108

Decatur County Hospital
A Component Unit of Decatur County, Kansas
Statements of Revenues, Expenses and Changes in Net Assets
Years Ended December 31, 2010 and 2009

	<u>2010</u>	<u>2009</u>
Operating Revenues		
Net patient service revenue, net of provision for uncollectible accounts; 2010 - \$214,592, 2009 - \$183,087	\$ 6,537,306	\$ 6,449,175
Other	<u>113,102</u>	<u>121,792</u>
Total operating revenues	<u>6,650,408</u>	<u>6,570,967</u>
Operating Expenses		
Salaries	3,557,707	3,476,001
Employee benefits	756,354	1,048,057
Purchased services	442,256	429,312
Drugs	474,583	468,718
Medical supplies	256,200	278,798
Food	110,815	125,336
Utilities	263,633	247,558
Repairs and maintenance	59,642	114,074
Professional fees	386,108	379,785
Dues	30,587	34,934
Insurance	52,465	58,859
Supplies and other	277,484	276,958
Depreciation	<u>209,624</u>	<u>316,272</u>
Total operating expenses	<u>6,877,458</u>	<u>7,254,662</u>
Operating Loss	<u>(227,050)</u>	<u>(683,695)</u>
Nonoperating Revenues (Expenses)		
Intergovernmental revenue	179,821	217,965
Net investment income	197,405	299,778
Interest expense	(34,898)	(29,951)
Noncapital gifts and grants	<u>28,894</u>	<u>40,747</u>
Total nonoperating revenues	<u>371,222</u>	<u>528,539</u>
Increase (Decrease) in Net Assets	144,172	(155,156)
Net Assets, Beginning of Year	<u>4,992,661</u>	<u>5,147,817</u>
Net Assets, End of Year	<u><u>\$ 5,136,833</u></u>	<u><u>\$ 4,992,661</u></u>

Decatur County Hospital
A Component Unit of Decatur County, Kansas
Statements of Cash Flows
Years Ended December 31, 2010 and 2009

	<u>2010</u>	<u>2009</u>
Operating Activities		
Receipts from and on behalf of patients	\$ 6,862,803	\$ 5,821,449
Payments to suppliers and contractors	(2,389,351)	(2,265,879)
Payments to or on behalf of employees	(4,266,821)	(4,515,875)
Other receipts, net	<u>156,565</u>	<u>121,792</u>
Net cash provided by (used in) operating activities	<u>363,196</u>	<u>(838,513)</u>
Noncapital Financing Activities		
Intergovernmental revenue	179,821	217,965
Noncapital gifts and grants	28,894	40,747
Proceeds from issuance of short-term debt	-	175,000
Principal paid on short-term debt	<u>(150,000)</u>	<u>(25,000)</u>
Net cash provided by noncapital financing activities	<u>58,715</u>	<u>408,712</u>
Capital and Related Financing Activities		
Proceeds from issuance of long-term debt	-	-
Payment of bond issuance costs	-	-
Principal paid on long-term debt	(53,044)	(54,767)
Interest paid on note payable to bank	(32,585)	(29,951)
Purchase of capital assets	<u>(259,913)</u>	<u>(419,527)</u>
Net cash used in capital and related financing activities	<u>(345,542)</u>	<u>(504,245)</u>
Investing Activities		
Net investment income	197,405	299,778
Net change in short-term certificates of deposit	-	982
Purchase of investments	<u>(160,414)</u>	<u>(252,382)</u>
Net cash provided by investing activities	<u>36,991</u>	<u>48,378</u>
Increase (Decrease) in Cash and Cash Equivalents	113,360	(885,668)
Cash and Cash Equivalents, Beginning of Year	<u>610,031</u>	<u>1,495,699</u>
Cash and Cash Equivalents, End of Year	<u><u>\$ 723,391</u></u>	<u><u>\$ 610,031</u></u>

Decatur County Hospital
A Component Unit of Decatur County, Kansas
Statements of Cash Flows (Continued)
Years Ended December 31, 2010 and 2009

	<u>2010</u>	<u>2009</u>
Reconciliation of Net Operating Revenues (Expenses) to Net Cash Provided by (Used in) Operating Activities		
Operating loss	\$ (227,050)	\$ (683,695)
Depreciation and amortization	209,624	316,272
Loss on disposal of assets	43,463	-
Changes in operating assets and liabilities		
Patient accounts receivable, net	(433,337)	122,274
Estimated amounts due from and to third-party payers	758,834	(750,000)
Supplies and prepaid expenses	(32,847)	18,478
Other assets	70,159	66,788
Accounts payable and accrued expenses	<u>(25,650)</u>	<u>71,370</u>
Net cash provided by (used in) operating activities	<u>\$ 363,196</u>	<u>\$ (838,513)</u>

Decatur County Hospital
A Component Unit of Decatur County, Kansas
Notes to Financial Statements
December 31, 2010 and 2009

Note 1: Nature of Operations and Summary of Significant Accounting Policies

Nature of Operations and Reporting Entity

Decatur County Hospital (Hospital) is an acute care hospital located in Oberlin, Kansas. The Hospital is a component unit of Decatur County, Kansas (County) and the Board of County Commissioners appoints members to the Board of Trustees of the Hospital. The Hospital primarily earns revenues by providing inpatient, outpatient and emergency care services to patients in the Decatur county area. It also operates a long-term care facility, outpatient clinic and home health agency in the same geographic area.

The Board of Trustees of Decatur County Hospital (Lessor) leases the Hospital's operations to Decatur Health Systems, Inc. (Lessee) (DHS) as a Section 501(c)(3) organization. The lease extends through December 31, 2028. Board members of the Lessor act as the Board of Trustees for the Lessee. At the conclusion of the lease, custody of all assets and liabilities reverts to the Lessor. Rent expense under this lease is \$5 per year plus any amounts due on debt incurred by the Lessor on Lessee's behalf for equipment or for operating purposes.

The financial statements include the accounts of the Hospital and DHS as a blended component unit of the Hospital. All significant intercompany accounts and transactions have been eliminated.

Basis of Accounting and Presentation

The financial statements of the Hospital have been prepared on the accrual basis of accounting using the economic resources measurement focus. Revenues, expenses, gains, losses, assets and liabilities from exchange and exchange-like transactions are recognized when the exchange transaction takes place, while those from government-mandated nonexchange transactions are recognized when all applicable eligibility requirements are met. Operating revenues and expenses include exchange transactions. Government-mandated nonexchange transactions that are not program specific such as intergovernmental revenue from property taxes, investment income and interest on capital assets-related debt are included in nonoperating revenues and expenses. The Hospital first applies restricted net assets when an expense or outlay is incurred for purposes for which both restricted and unrestricted net assets are available.

The Hospital prepares its financial statements as a business-type activity in conformity with applicable pronouncements of the Governmental Accounting Standards Board (GASB). Pursuant to GASB Statement No. 20, the Hospital has elected to apply the provisions of all relevant pronouncements of the Financial Accounting Standards Board (FASB) that were issued on or before November 30, 1989, and do not conflict with or contradict GASB pronouncements.

Decatur County Hospital
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Notes to Financial Statements
December 31, 2010 and 2009

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Cash Equivalents

The Hospital considers all liquid investments with original maturities of three months or less to be cash equivalents. At December 31, 2010 and 2009, cash equivalents consisted of certificates of deposit with maturities of less than 90 days.

Intergovernmental Revenue

The Hospital received approximately 3% in both 2010 and 2009, of its financial support from property taxes levied by the County and shared with the Hospital for hospital purposes. One hundred percent of these funds were used to support operations in both years.

Taxes are assessed by the County in November and are received beginning in January of each year. Intergovernmental revenue is recognized in full in the year in which use is first permitted.

Risk Management

The Hospital is exposed to various risks of loss from torts; theft of, damage to and destruction of assets; business interruption; errors and omissions; employee injuries and illnesses; natural disasters; and employee health, dental and accident benefits. Commercial insurance coverage is purchased for claims arising from such matters other than health benefits and workers' compensation. A partially self-funded health insurance plan covers medical services up to a certain amount after which point commercial insurance coverage provides the remaining coverage. Management believes adequate reserves are in place to cover claims incurred but not reported at year-end. Workers' compensation coverage is provided through a fund managed by the Kansas Workers' Risk Cooperative for Counties. The workers' compensation premiums are subject to retrospective adjustment based upon the overall performance of the fund. Management believes adequate reserves are in place to cover claims incurred but not reported for workers' compensation.

The partially self-insured health and dental insurance plan covers medical and dental services up to \$25,000 per individual. Claims in excess of \$25,000 per individual are covered through a reinsurance policy. Management believes adequate accruals are in place to cover claims under \$25,000 which have been incurred but not reported.

Decatur County Hospital
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Notes to Financial Statements
December 31, 2010 and 2009

Patient Accounts Receivable

The Hospital reports patient accounts receivable for services rendered at net realizable amounts from third-party payers, patients and others. The Hospital provides an allowance for uncollectible accounts based upon a review of outstanding receivables, historical collection information and existing economic conditions.

Supplies

Supply inventories are stated at the lower of cost, determined using the first-in, first-out method, or market.

Capital Assets

Capital assets are recorded at cost at the date of acquisition, or fair value at the date of donation if acquired by gift. Depreciation is computed using the straight-line method over the estimated useful life of each asset. The following estimated useful lives are being used by the Hospital:

Land improvements	5 - 20 years
Buildings and building improvements	3 - 21 years
Fixed equipment	8 - 20 years
Major moveable equipment	3 - 15 years

Compensated Absences

Hospital policies permit most employees to accumulate vacation, holiday, personal and sick leave benefits that may be realized as paid time off or as a cash payment. Expense and the related liability are recognized as benefits are earned whether the employee is expected to realize the benefit as time off or in cash. Compensated absence liabilities are computed using the regular pay rate in effect at the balance sheet date plus an additional amount for compensation-related payments such as social security and Medicare taxes computed using rates in effect at that date.

Deferred Revenue

Deferred revenue consists of grant monies received for specific purposes. Revenue is recognized on deferred grant revenue when specific purpose of grant is met.

Decatur County Hospital
A Component Unit of Decatur County, Kansas
Notes to Financial Statements
December 31, 2010 and 2009

Net Assets

Net assets of the Hospital are classified in three components. Net assets invested in capital assets, net of related debt, consist of capital assets net of accumulated depreciation and reduced by the outstanding balances of borrowings used to finance the purchase or construction of those assets. Restricted expendable net assets are noncapital assets that must be used for a particular purpose as specified by creditors, grantors or donors external to the Hospital, including amounts deposited with trustees as required by bond indentures, reduced by the outstanding balances of any related borrowings. Unrestricted net assets are remaining assets less remaining liabilities that do not meet the definition of invested in capital assets, net of related debt or restricted expendable.

Net Patient Service Revenue

The Hospital has agreements with third-party payers that provide for payments to the Hospital at amounts different from its established rates. Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payers and others for services rendered and includes estimated retroactive revenue adjustments and a provision for uncollectible accounts. Retroactive adjustments are considered in the recognition of revenue on an estimated basis in the period the related services are rendered and such estimated amounts are revised in future periods as adjustments become known.

Charity Care

The Hospital provides care without charge or at amounts less than its established rates to patients meeting certain criteria under its charity care policy. Because the Hospital does not pursue collection of amounts determined to qualify as charity care, these amounts are not reported as net patient service revenue.

Income Taxes

As an essential government function of the County, the Hospital is generally exempt from federal and state income taxes under Section 115 of the Internal Revenue Code and a similar provision of state law. DHS is exempt from income taxes under Section 501 of the Internal Revenue Code and a similar provision of state law. However, both entities are subject to federal income tax on any unrelated business taxable income.

Subsequent Events

Subsequent events have been evaluated through April 12, 2011, which is the date the financial statements were available to be issued.

Decatur County Hospital
A Component Unit of Decatur County, Kansas
Notes to Financial Statements
December 31, 2010 and 2009

Note 2: Net Patient Service Revenue

The Hospital has agreements with third-party payers that provide for payments to the Hospital at amounts different from its established rates. These payment arrangements include:

Medicare. The Hospital is recognized as a Critical Access Hospital (CAH). Under CAH rules, inpatient acute care, skilled swing-bed and outpatient services rendered to Medicare program beneficiaries are paid at one hundred one percent (101%) of allowable cost subject to certain limitations. The Hospital is reimbursed for certain services at tentative rates with final settlement determined after submission of annual cost reports by the Hospital and audits thereof by the Medicare administrative contractor.

Medicaid. The Medicaid State Plan provides for a cost reimbursement methodology for inpatient and outpatient services rendered to beneficiaries who are not part of a Medicaid managed care network. The Hospital is reimbursed at tentative rates with final settlements determined after submission of annual cost reports and reviews thereof by the Kansas Health Policy Authority (KHPA). The Hospital is reimbursed on a prospective payment methodology for inpatient and outpatient services rendered to beneficiaries who are part of a Medicaid managed care network.

Medicaid reimbursement for long-term care facility residents is based on a cost-based prospective reimbursement methodology. The Hospital is reimbursed at a prospective rate with annual cost reports submitted to the Medicaid program. Rates are computed each calendar quarter using an average of the 2005, 2006 and 2007 cost reports and changes in the Medicaid resident case mix index. The Medicaid cost reports are subject to audit by the State and adjustments to rates can be made retroactively.

Approximately 64% and 63% of net patient service revenue is from participation in the Medicare and state-sponsored Medicaid programs for the years ended December 31, 2010 and 2009, respectively. Laws and regulations governing the Medicare and Medicaid programs are complex and subject to interpretation and change. As a result, it is reasonably possible that recorded estimates will change materially in the near term.

The Hospital has also entered into payment agreements with certain commercial insurance carriers and preferred provider organizations. The basis for payment to the Hospital under these agreements includes prospectively determined rates per discharge and discounts from established charges.

Decatur County Hospital
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Notes to Financial Statements
December 31, 2010 and 2009

Note 3: Deposits and Interest Income

Deposits

Custodial credit risk is the risk that in the event of a bank failure, a government's deposits may not be returned to it. The Hospital's deposit policy for custodial credit risk requires compliance with the provisions of state law.

State law requires collateralization of all deposits with federal depository insurance; bonds and other obligations of the U.S. Treasury, U.S. agencies or instrumentalities or the state of Kansas; bonds of any city, county, school district or special road district of the state of Kansas; bonds of any state; or a surety bond having an aggregate value at least equal to the amount of the deposits.

At December 31, 2010 and 2009, respectively, \$411,050 and \$519,631 of the Hospital's bank balances of \$917,288 and \$1,025,823 were exposed to custodial credit risk as follows:

	2010	2009
Uninsured and collateral held by pledging financial institution's trust department or agent in other than the Hospital's name	<u>\$ 411,050</u>	<u>\$ 519,631</u>

Summary of Carrying Values

The carrying values of deposits above are included in the balance sheets as follows:

	2010	2009
Carrying value		
Deposits	\$ 920,885	\$ 1,029,579
Deposits held by a nongovernmental entity - DHS	<u>312,454</u>	<u>90,400</u>
	<u>\$ 1,233,339</u>	<u>\$ 1,119,979</u>
Included in the following balance sheet captions		
Cash and cash equivalents	\$ 723,391	\$ 610,031
Short-term certificates of deposit	<u>509,948</u>	<u>509,948</u>
	<u>\$ 1,233,339</u>	<u>\$ 1,119,979</u>

Decatur County Hospital
A Component Unit of Decatur County, Kansas
Notes to Financial Statements
December 31, 2010 and 2009

Note 4: Patient Accounts Receivable

The Hospital grants credit without collateral to its patients, many of whom are area residents and are insured under third-party payer agreements. Patient accounts receivable at December 31, 2010 and 2009, consisted of:

	2010	2009
Medicare	\$ 846,298	\$ 512,093
Medicaid	105,336	87,657
Blue Cross	111,731	63,245
Other third-party payers	137,000	95,448
Patients	470,205	448,790
	<u>1,670,570</u>	<u>1,207,233</u>
Less allowance for uncollectible accounts	<u>402,000</u>	<u>372,000</u>
	<u><u>\$ 1,268,570</u></u>	<u><u>\$ 835,233</u></u>

Note 5: Investments and Long-term Deposit

Interest in Assets of Decatur Health Care Foundation, Inc.

The Hospital has transferred assets (cash) to the Decatur Health Care Foundation, Inc. (Foundation) and retained a beneficial interest in those assets. Earnings on the funds held by the Foundation are to be remitted to the Hospital, and the principal can be invaded in extreme financial circumstances as determined jointly by the boards of both organizations. Currently, the funds held by the Foundation are invested in certificates of deposit and mutual funds.

Option Deposit

On February 4, 2004, DHS entered into an agreement with Decatur County Retirement Housing, Inc. (DCRHI) to manage the Wheat Ridge Terrace independent living units. The management agreement calls for DHS to provide meals, maintenance, housekeeping and administrative services for a fee. Actual costs are used to determine the fees charged. As part of the agreement, DHS invested \$250,000 to assist DCRHI in restructuring its debt. In return, DHS has the option of acquiring the assets of DCRHI when all outstanding debt of DCRHI is paid.

Decatur County Hospital
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Notes to Financial Statements
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Note 6: Capital Assets

Capital assets activity for the years ended December 31, 2010 and 2009, was:

	2010			
	Beginning Balance	Additions	Disposals	Ending Balance
Land improvements	\$ 199,569	\$ -	\$ -	\$ 199,569
Buildings and building improvements	3,700,284	-	-	3,700,284
Fixed equipment	516,111	250,312	(71,939)	694,484
Major moveable equipment	<u>1,991,329</u>	<u>9,601</u>	<u>-</u>	<u>2,000,930</u>
	<u>6,407,293</u>	<u>259,913</u>	<u>(71,939)</u>	<u>6,595,267</u>
Less accumulated depreciation				
Land improvements	114,444	9,536	-	123,980
Buildings and building improvements	2,851,720	39,260	-	2,890,980
Fixed equipment	92,492	77,819	(28,476)	141,835
Major moveable equipment	<u>1,642,843</u>	<u>82,634</u>	<u>-</u>	<u>1,725,477</u>
	<u>4,701,499</u>	<u>209,249</u>	<u>(28,476)</u>	<u>4,882,272</u>
Capital assets, net	<u><u>\$ 1,705,794</u></u>	<u><u>\$ 50,664</u></u>	<u><u>\$ (43,463)</u></u>	<u><u>\$ 1,712,995</u></u>

Decatur County Hospital
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Notes to Financial Statements
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	2009				
	Beginning Balance	Additions	Disposals	Transfers	Ending Balance
Land improvements	\$ 199,569	\$ -	\$ -	\$ -	\$ 199,569
Buildings and building improvements	3,655,244	45,040	-	-	3,700,284
Fixed equipment	180,209	335,902	-	-	516,111
Major moveable equipment	<u>1,952,744</u>	<u>38,585</u>	<u>-</u>	<u>-</u>	<u>1,991,329</u>
	<u>5,987,766</u>	<u>419,527</u>	<u>-</u>	<u>-</u>	<u>6,407,293</u>
Less accumulated depreciation					
Land improvements	104,909	9,535	-	-	114,444
Buildings and building improvements	2,723,109	128,611	-	-	2,851,720
Fixed equipment	49,784	42,708	-	-	92,492
Major moveable equipment	<u>1,507,800</u>	<u>135,043</u>	<u>-</u>	<u>-</u>	<u>1,642,843</u>
	<u>4,385,602</u>	<u>315,897</u>	<u>-</u>	<u>-</u>	<u>4,701,499</u>
Capital assets, net	<u>\$ 1,602,164</u>	<u>\$ 103,630</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$1,705,794</u>

Note 7: Accounts Payable and Accrued Expenses

Accounts payable and accrued expenses included in current liabilities at December 31, 2010 and 2009, consisted of:

	2010	2009
Payable to suppliers and contractors	\$ 155,695	\$ 228,585
Payable to employees (including payroll taxes and benefits)	488,404	436,651
Other	<u>-</u>	<u>2,200</u>
	<u>\$ 644,099</u>	<u>\$ 667,436</u>

Decatur County Hospital
A Component Unit of Decatur County, Kansas
Notes to Financial Statements
December 31, 2010 and 2009

Note 8: Self-insured Health Insurance

Substantially all of the Hospital's employees and their dependents are eligible to participate in the Hospital's employee health insurance plan. The Hospital was self-insured for health claims of participating employees and dependents up to an annual aggregate amount of \$25,000 per covered employee. Commercial stop-loss insurance coverage is purchased for claims in excess of the aggregate annual amount. A provision is accrued for self-insured employee health claims including both claims reported and claims incurred but not yet reported. The accrual is estimated based on consideration of prior claims experience, recently settled claims, frequency of claims and other economic and social factors. It is reasonably possible that the Hospital's estimate will change by a material amount in the near term.

Activity in the Hospital's accrued employee health claims liability during 2010 and 2009 is summarized as follows:

	2010	2009
Balance, beginning of year	\$ 64,054	\$ 92,345
Current year claims incurred and changes in estimates for claims incurred in prior years	329,314	632,830
Claims and expenses paid	<u>(329,314)</u>	<u>(661,121)</u>
Balance, end of year	<u><u>\$ 64,054</u></u>	<u><u>\$ 64,054</u></u>

Note 9: Note Payable to Bank

DHS borrowed funds from a bank to finance Hospital operations on an interim basis through a line of credit, which has a maximum of \$150,000 of available funds. The note payable bore interest at 6.50% and 9.50% for 2010 and 2009, was unsecured and matured in less than one year from issuance. The following is a summary of short-term note payable transactions for the years ended December 31, 2010 and 2009:

	2010	2009
Beginning balance	\$ 150,000	\$ -
Additions	-	175,000
Payments	<u>(150,000)</u>	<u>(25,000)</u>
Ending balance	<u><u>\$ -</u></u>	<u><u>\$ 150,000</u></u>

Decatur County Hospital
A Component Unit of Decatur County, Kansas
Notes to Financial Statements
December 31, 2010 and 2009

Note 10: Medical Malpractice Claims

The Hospital purchases medical malpractice insurance under a claims-made policy with a fixed premium which provides \$200,000 of coverage for each medical incident and \$600,000 of aggregate coverage for each policy year. The policy only covers claims made and reported to the insurer during the policy term, regardless of when the incident giving rise to the claim occurred. The Kansas Health Care Stabilization Fund provides an additional \$800,000 of coverage for each medical incident and \$2,400,000 of aggregate coverage for each policy year.

Accounting principles generally accepted in the United States of America require a health care provider to accrue the expense of its share of malpractice claim costs, if any, for any reported and unreported incidents of potential improper professional service occurring during the year by estimating the probable ultimate costs of the incidents. Based upon the Hospital's claims experience, no such accrual has been made. It is reasonably possible that this estimate could change materially in the near term.

Note 11: Direct Financing Leases

The Hospital has provided direct financing leases for equipment used by local physicians. These leases require monthly payments and generally range from one to five years.

Future minimum lease payments receivable at December 31, 2010, were:

2011	\$ 17,236
Future minimum lease payments receivable	<u>17,236</u>
Less amounts representing interest	<u>1,582</u>
	15,654
Less current portion	<u>15,654</u>
	<u><u>\$ -</u></u>

Decatur County Hospital
A Component Unit of Decatur County, Kansas
Notes to Financial Statements
December 31, 2010 and 2009

Note 12: Long-term Debt

The following is a summary of long-term debt transactions for the Hospital for the years ended December 31, 2010 and 2009:

	2010				
	Beginning Balance	Additions	Payments	Ending Balance	Current Portion
Note payable - county - 2002 (A)	\$ 60,000	\$ -	\$ (20,000)	\$ 40,000	\$ 20,000
Note payable - county - 2003 (B)	45,484	-	(10,612)	34,872	11,103
Note payable - county - 2008 (C)	628,527	-	(22,432)	606,095	23,358
Total long-term debt	<u>\$ 734,011</u>	<u>\$ -</u>	<u>\$ (53,044)</u>	<u>\$ 680,967</u>	<u>\$ 54,461</u>

	2009				
	Beginning Balance	Additions	Payments	Ending Balance	Current Portion
Note payable - county - 2002 (A)	\$ 80,000	\$ -	\$ (20,000)	\$ 60,000	\$ 20,000
Note payable - county - 2003 (B)	55,627	-	(10,143)	45,484	10,612
Note payable - county - 2008 (C)	650,000	-	(21,473)	628,527	22,432
Lease payable	3,151	-	(3,151)	-	-
Total long-term debt	<u>\$ 788,778</u>	<u>\$ -</u>	<u>\$ (54,767)</u>	<u>\$ 734,011</u>	<u>\$ 53,044</u>

Note Payable – County – 2002 (A)

The note payable – county – 2002 consists of an agreement with the County to repay on its behalf the General Obligation Bonds, Series 2002-A (Bonds) in the original amount of \$200,000 dated July 2, 2002. These Bonds were purchased in their entirety by Prairie Land Electric Cooperative, Inc. at their par value with no interest due on these Bonds pursuant to a Rural Economic Development Loan and Grant Program. The proceeds from this loan were used to finance equipment purchases. The Bonds are payable in annual installments through July 17, 2012. The Hospital is required to make annual payments of \$20,000 to the debt service fund held by the trustee.

Decatur County Hospital
A Component Unit of Decatur County, Kansas
Notes to Financial Statements
December 31, 2010 and 2009

The debt service requirements as of December 31, 2010, are as follows:

Year Ending December 31,	Total to be Paid	Principal	Interest
2011	\$ 20,000	\$ 20,000	\$ -
2012	<u>20,000</u>	<u>20,000</u>	<u>-</u>
	<u>\$ 40,000</u>	<u>\$ 40,000</u>	<u>\$ -</u>

Note Payable – County – 2003 (B)

The note payable – county – 2003 consists of an agreement with the County to repay on its behalf the General Obligation Bonds, Series 2003, (Bonds) in the original amount of \$100,000 dated March 18, 2003, which bear interest at 4.625%. The proceeds from this loan were used to finance equipment purchases. The Bonds are payable in annual installments through April 1, 2013. The Hospital is required to make annual payments of approximately \$12,716 to the debt service fund held by the trustee. The Bonds are secured by the net revenues and accounts receivable of the Hospital. The debt service requirements as of December 31, 2010, are as follows:

Year Ending December 31,	Total to be Paid	Principal	Interest
2011	\$ 12,716	\$ 11,103	\$ 1,613
2012	12,716	11,616	1,100
2013	<u>12,716</u>	<u>12,153</u>	<u>563</u>
	<u>\$ 38,148</u>	<u>\$ 34,872</u>	<u>\$ 3,276</u>

Note Payable – County – 2008 (C)

The note payable – county – 2008 consists of an agreement with the County to repay on its behalf the Revenue Bonds, Series 2008, (Bonds) in the original amount of \$650,000 dated February 22, 2008, which bear interest at 4.125%. The proceeds from this loan were used to finance construction of a specialty clinic. The Bonds are payable in annual installments through February 22, 2028. The Hospital is required to make annual payments of approximately \$48,359 to the debt service fund held by the trustee. The Bonds are secured by the net revenues and accounts receivable of the Hospital. The agreement also includes certain financial covenants which, among other things, require monthly deposits of principal and interest payments into a separate Debt Service Account, to the extent necessary to meet on each payment date the payment of all interest and principal. The Hospital did not meet the required deposit covenants during 2010.

Decatur County Hospital
A Component Unit of Decatur County, Kansas
Notes to Financial Statements
December 31, 2010 and 2009

The debt service requirements as of December 31, 2010, are as follows:

Year Ending December 31,	Total to be Paid	Principal	Interest
2011	\$ 48,359	\$ 23,358	\$ 25,001
2012	48,359	24,321	24,038
2013	48,359	25,261	23,098
2014	48,359	26,366	21,993
2015	48,359	27,454	20,905
2016-2020	241,795	155,163	86,632
2021-2025	241,795	189,911	51,884
2026-2028	145,504	134,261	11,243
	<u>\$ 870,889</u>	<u>\$ 606,095</u>	<u>\$ 264,794</u>

Note 13: Restricted and Designated Net Assets

At December 31, 2010 and 2009, restricted expendable net assets of \$48,786 were available for debt service.

At December 31, 2010 and 2009, respectively, \$73,717 and \$67,171 of unrestricted net assets have been designated by the Hospital's Board of Trustees for capital acquisitions. Designated net assets remain under the control of the Board of Trustees, which may at its discretion later use these net assets for other purposes.

Note 14: Related Party Transactions

An officer of a local financial institution is also a member of the Board of Trustees. At December 31, 2010 and 2009, the Hospital had cash balances of approximately \$597,000 and \$550,000, respectively, on deposit with this financial institution.

Note 15: Pension Plan

The Hospital contributes to a defined contribution pension plan covering substantially all employees. Pension expense is recorded for the amount of the Hospital's required contributions, determined in accordance with the terms of the plan. The plan is administered by the Hospital Board of Trustees. The plan provides retirement benefits to plan members and their beneficiaries. Benefit provisions are contained in the plan document and were established and can be amended by

Decatur County Hospital
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Notes to Financial Statements
December 31, 2010 and 2009

action of the Hospital's governing body. Contribution rates for plan members and the Hospital expressed as a percentage of covered payroll were 4.4% and 2.3% for 2010, 4.1% and 2.2% for 2009, and 4.6% and 2.4% for 2008, respectively. Contributions actually made by plan members and the Hospital aggregated \$156,775 and \$82,161 during 2010, \$143,465 and \$77,995 during 2009, and \$149,247 and \$78,253 during 2008, respectively.

Note 16: Contingencies

Litigation

In the normal course of business, the Hospital is, from time to time, subject to allegations that may or do result in litigation. Some of these allegations are in areas not covered by the Hospital's commercial insurance; for example, allegations regarding employment practices or performance of contracts. The Hospital evaluates such allegations by conducting investigations to determine the validity of each potential claim. Based upon the advice of legal counsel, management records an estimate of the amount of ultimate expected loss, if any, for each. Events could occur that would cause the estimate of ultimate loss to differ materially in the near term.

Note 17: Significant Estimates and Concentrations

Current Economic Conditions

The current protracted economic decline continues to present hospitals with difficult circumstances and challenges, which in some cases have resulted in large and unanticipated declines in assets, large declines in contributions, constraints on liquidity and difficulty obtaining financing. The financial statements have been prepared using values and information currently available to the Hospital.

Current economic conditions, including the rising unemployment rate, have made it difficult for certain of our patients to pay for services rendered. As employers make adjustments to health insurance plans or more patients become unemployed, services provided to self-pay and other payers may significantly impact net patient service revenue, which could have an adverse impact on the Hospital's future operating results. Further, the effect of economic conditions on the government may have an adverse effect on cash flows related to the Medicare and Medicaid programs.

Given the volatility of current economic conditions, the values of assets and liabilities recorded in the financial statements could change rapidly, resulting in material future adjustments in allowances for accounts receivable that could negatively impact the Hospital's ability to maintain sufficient liquidity.

Decatur County Hospital
A Component Unit of Decatur County, Kansas
Notes to Financial Statements
December 31, 2010 and 2009

Note 18: Subsequent Events

Medicaid Provider Assessment

On February 2, 2011, the Centers for Medicare and Medicaid Services (CMS) approved a Medicaid State Plan amendment which provides for additional funds to be paid to operators of long-term care facilities. The Kansas Department on Aging has estimated the additional net receipts for the Hospital to be approximately \$98,000. These receipts are expected to begin in March 2011.

Purchase of Oberlin Medical Arts

Effective April 2011, the Hospital acquired the physician practice of the Oberlin Medical Arts for a total purchase price of \$145,000.

Supplementary Information

Decatur County Hospital
A Component Unit of Decatur County, Kansas
Balance Sheets of Decatur Health Systems, Inc.
December 31, 2010 and 2009

Assets

	<u>2010</u>	<u>2009</u>
Current Assets		
Cash	\$ 312,454	\$ 90,400
Patient accounts receivable, net of allowance; 2010 - \$402,000, 2009 - \$372,000	1,268,570	835,233
Other receivables	17,191	56,506
Estimated amounts due from third-party payers	-	480,000
Supplies	104,962	89,511
Prepaid expenses and other	<u>47,974</u>	<u>30,578</u>
Total current assets	<u>1,751,151</u>	<u>1,582,228</u>
Option Deposit	<u>250,000</u>	<u>250,000</u>
Capital Assets, At Cost		
Property and equipment	1,057,453	1,047,852
Less accumulated depreciation	<u>874,950</u>	<u>812,642</u>
	<u>182,503</u>	<u>235,210</u>
Total assets	<u><u>\$ 2,183,654</u></u>	<u><u>\$ 2,067,438</u></u>

Liabilities and Net Assets

	2010	2009
Current Liabilities		
Line of credit	\$ -	\$ 150,000
Accounts payable	155,695	177,670
Accrued payroll and related deductions	243,617	216,493
Accrued vacation pay	155,535	133,219
Accrued expenses	64,054	64,054
Estimated amounts due to third-party payers	278,834	-
Deferred revenue	-	2,200
	<hr/>	<hr/>
Total current liabilities	897,735	743,636
 Due to Lessor	 1,285,919	 1,323,802
	<hr/>	<hr/>
Total liabilities	2,183,654	2,067,438
	<hr/>	<hr/>
Unrestricted Net Assets	-	-
	<hr/>	<hr/>
Total liabilities and net assets	\$ 2,183,654	\$ 2,067,438
	<hr/> <hr/>	<hr/> <hr/>

Decatur County Hospital
A Component Unit of Decatur County, Kansas
Statements of Operations of Decatur Health Systems, Inc.
Years Ended December 31, 2010 and 2009

	<u>2010</u>	<u>2009</u>
Revenues, Gains and Other Support		
Net patient service revenue	\$ 6,751,898	\$ 6,632,262
Other revenue	<u>101,102</u>	<u>107,669</u>
	<u>6,853,000</u>	<u>6,739,931</u>
Expenses		
Salaries and wages	3,557,707	3,476,001
Employee benefits	756,354	1,048,057
Purchased services	442,256	429,312
Drugs	474,583	468,718
Medical supplies	256,200	278,798
Food	110,815	125,336
Utilities	263,633	247,558
Repairs and maintenance	51,925	60,738
Professional fees	383,950	374,394
Dues	30,587	34,934
Insurance	48,930	55,469
Other supplies and expenses	211,962	238,650
Interest	4,617	641
Depreciation	62,308	106,083
Provision for uncollectible accounts	<u>214,592</u>	<u>183,087</u>
	<u>6,870,419</u>	<u>7,127,776</u>
Operating Loss	<u>(17,419)</u>	<u>(387,845)</u>
Other Income		
Interest income	5,994	8,097
Noncapital gifts and grants	<u>56,819</u>	<u>219,703</u>
	<u>62,813</u>	<u>227,800</u>
Increase (Decrease) in Net Assets	45,394	(160,045)
Change in Amount Due to Lessor	<u>(45,394)</u>	<u>160,045</u>
Change in Unrestricted Net Assets	<u>\$ -</u>	<u>\$ -</u>